

FEDERAL TRADE COMMISSION

**P2P FILE SHARING WORKSHOP -- REQUEST TO
PARTICIPATE, PO34517**

AND

COMMENTS

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FILED BY:

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REQUEST TO PARTICIPATE AS PANELIST

James V. DeLong is a Senior Fellow at The Progress & Freedom Foundation (PFF), a non-profit research and educational institution as defined by the Code of the Internal Revenue Service, 26 U.S.C. § 501(c)(3). The foundation's principle mission is to study the impact of the digital revolution and its impact on public policy.

Mr. DeLong is also the Director of the Center for the Study of Digital Property, which is a special project within PFF dedicated to developing and advancing market-based, property-rights-oriented approaches to issues of digital content.

In furtherance of its mission, the Center maintains a website entitled *IPcentral.Info*, [www.ipcentral.info] which contains links to a variety of materials on intellectual property issues, including written materials, a weblog, and links to other sites with related interests. Fellows associated with the CSDP prepare analyses of important intellectual property issues, including, earlier this year, a paper on "Liability of P2P File-Sharing Systems for Copyright Infringement By Their Users."¹ Fellows have testified in front of Congress and interact regularly with journalists, academicians, industry representatives, and government officials.

Mr. DeLong served in the Bureau of Consumer Protection of the Federal Trade Commission from 1974 to 1978. He was successively Assistant Director for Special Projects and Associate Director for Policy Planning.

The Division of Special Projects had been created for the precise purpose of developing theories that would define and structure the Commission's authority to act against "unfair" (as distinguished from "deceptive") acts or practices, after this power was blessed by the Supreme Court in the *S&H case*.² At various times, Mr. DeLong supervised the Commission's proceedings in such matters as vocational schools, prescription drugs, ophthalmic goods and services, credit practices, and even advertising to children.

He also acted as the Chair of an informal group called the Ad Hoc Committee on Unfairness, which was charged with creating theories of "unfairness" that could compare in intellectual rigor with theories of antitrust law. The group disbanded after the change of administrations in 1977, so its efforts bore no formal fruit, but it was a serious effort to deal with some difficult problems.

Because of his experience, Mr. DeLong is intimately familiar with the history of the Commission's exercise of its authority to act against "unfair acts or practices," and is in a unique position to comment on possible applications of that authority to the issue of file-sharing over P2P networks.

¹ William F. Adkinson, Jr., "Liability of P2P File-Sharing Systems for Copyright Infringement By Their Users," The Progress & Freedom Foundation, *Progress on Point* No. 11.7 (March 2004) (available at

² *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233 (1972).

COMMENTS

The FTC has authority under 15 U.S.C. 45 to act against "unfair . . . acts or practices" that "cause[] or [are] likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition."³

The Commission should seriously consider invoking this authority to curb many of the practices engaged in by Internet services that are relying on P2P technology.

The Commission has already recognized that some P2P services may not adequately apprise consumers of the risks associated with the use of P2P networks. This was the subject of congressional testimony given by the Director of the Bureau of Consumer Protection last June, in which he emphasized that the Commission would continue to watch this area.⁴

A related area is the constellation of practices identified by the Honorable Marybeth Peters, Register of Copyrights, in recent testimony before the Senate Committee on the Judiciary.⁵ She noted that to a large degree the success of P2P network services depends on the downloading of copyrighted materials to generate eyeballs that can then be sold to advertisers depend upon default settings and other practices that rope the user into full participation in the system. For example, "Kazaa has programmed into its software [a number of steps] to make sure the user is 'sharing' as many files as possible." She quotes the Berkman Center at Harvard on some of these:

- "[B]y default, Kazaa starts itself immediately when the user turns on his computer. The program runs in the background, pre-set with the filesharing feature turned 'on' and configured to allow an unlimited number of uploads at a time. Many users may not be aware that the program is running continuously in this fashion.
- "When a user downloads a file from another Kazaa user, by default that copy is stored in the publicly shared folder, which means that it becomes immediately available for copying by others on the Kazaa network. Kazaa defaults to creating a shortcut to open this folder on the user's desktop; however the user may not be aware where exactly the folder itself is located on his computer.
- "Unlike most computer applications, clicking on the 'x' button on the top right-hand corner of the Kazaa program does not shut down Kazaa. This

³ 15 U.S.C. §§ 45(a) & 45(n).

⁴ J. Howard Beales, III, Director of BCP, FTC, Statement Before the Subcommittee on Competition, Infrastructure, and Foreign Commerce of the Committee on Commerce, Science, and Transportation, United States Senate, Hearing on P2P File-Sharing Technology, June 23, 2004.

⁵ Marybeth Peters, Register of Copyrights and Associate Librarian for Copyright Services, United States Copyright Office, Testimony Before the Committee on the Judiciary, United States Senate, on S. 2560, the Intentional Inducement of Copyright Infringements Act of 2004, July 22, 2004,

action merely hides the Kazaa program from the screen while the program continues to run the program in the background. To actually shut down the program, the user must then right-click the Kazaa icon located in Windows taskbar and choose the 'close' option.

- "Disabling the default file-sharing features in Kazaa is a complicated process due to an intricate series of steps within the software itself. In addition, the available resources that detail how to disable file sharing are often inconsistent or provide incomplete instructions.
- "It can be extremely difficult for a non-expert computer user to shut down their file-sharing capability."

Ms Peters adds that:

- "That difficulty is not an accident – it is the intentional design of the proprietors of these services. The defendants also affirmatively encourage people to distribute as many files as possible, knowing that most people will share infringing files. Kazaa implements what it calls 'Participation Levels', which increase a user's download performance based on the amount uploaded from that user. In other words, the more attractive the files you are sharing with other, the easier it will be for you to download copies from others. Indeed, Kazaa suggests that the user 'share large and interesting files.' This feature encourages users to make available popular copyrighted works, which will likely be the most frequently downloaded by others.
- "The proprietors of these services employ strategies of 'plausible deniability' and 'disaggregat[ing] functions' to avoid legal liability but allow copyright infringement on their networks to continue. As one attorney for these services explained:

'Can you plausibly deny what your users are up to? ... Have you built a level of 'plausible deniability' into your product architecture? If you promote, endorse, or facilitate the use of your product for infringing activity, you're asking for trouble. 'Software that sends back user reports may lead to more knowledge than you want. 'Customer support channels can also create bad "knowledge" evidence. Instead, talk up your great legitimate capabilities, sell it (or give it away), and then leave the users alone.

'Disaggregate functions ... In order to be successful, peer-to-peer networks will require products to address numerous functional needs—search, namespace management, security, dynamic file redistribution, to take a few examples. There's no reason why one entity should try to do all of these things. ...

'This approach may also have legal advantages. If Sony had not only manufactured VCRs, but also sold all the blank video tape, distributed all the TV Guides, and sponsored clubs and swap meets for VCR users, the Betamax case might have turned out differently. ...

'A disaggregated model, moreover, may limit what a court can order you to do to stop infringing activity by your users.' "⁶

These practices go far beyond a failure to explain risk adequately that was the focus of the recent Commission testimony. They represent a calculated program to induce consumers to enter into a massive system of mutually reinforcing piracy. In its recent notice on Ophthalmic Practices, the Commission reaffirmed the unfairness of some relatively mild practices that might conceivably cause consumers to spend a few extra dollars.⁷ These practices are pallid in comparison with what goes on in the P2P world. Indeed, the P2P world bears a resemblance to the *Zuccarini* case, in which the defendant more or less took control of the consumers' computers.⁸

A third possible use of the Commission's unfairness jurisdiction is more fundamental. PFF recently filed an *amicus* brief supporting the Petition for Certiorari in *MGM Studios Inc. v. Grokster*.⁹ The brief pointed out that consumers have serious Prisoner's Dilemma problem.

They know that unauthorized downloading of music is, in the long run, a devil's bargain for consumers. They may get material now, but because artists and middlemen do not get rewarded, the founts of creativity will inevitably dry up. At the same time, no individual consumer can stop the tide. So each individual has an incentive to continue a practice that all know will lead to collective disaster in the end.

The P2P services are taking advantage of this by building businesses that are infringement dependent. They can make money out of advertising or fees only because they do not pay for their raw material. But, in the end, consumers will be left with a dearth of new material, and, perhaps worse, with no legitimate structures of Internet distribution in place that *do* reward artists and middlemen and that would be capable of restarting the creative engine.

Such an action clearly meets the first test of unfairness, as laid out by Bureau Director Howard Beales in his excellent history of the FTC's unfairness doctrine delivered in a speech last year.¹⁰ And it fits with some of the concepts considered by the Ad Hoc Committee nigh onto 30 years ago, when we considered as possible bases for unfairness such practices (when coupled with serious injury) as systematic violation of common law rights and excessive departure from reasonable consumer expectations. Services that cynically rely on the decimation of consumers' long-term interests because they have

⁶ The author quoted is Fred von Lohmann, Electronic Frontier Foundation, "IAAL [I am a Lawyer]: What Peer-to-Peer Developers Need to Know about Copyright Law", § V.7 (December 2003) http://www.eff.org/IP/P2P/p2p_copyright_wp.php.]

⁷ FTC, Final Rule: Ophthalmic Practices, 69 *Fed. Reg.* 5451 (Feb. 4, 2004).

⁸ *FTC v. Zuccarini*, 2002-1 Trade Cas. (CCH) P73,690 (E.D. Pa. 2002).

⁹ 380 F.3d 1154 (9th Cir. 2004).

¹⁰ J. Howard Beales, III, Director of BCP, FTC, *The FTC's Use of Unfairness Authority: Its Rise, Fall, and Resurrection*, Speech given at the Marketing and Public Policy Conference, Washington, DC, May 30, 2003. <http://www.ftc.gov/speeches/beales/unfair0603.htm>

found a way to systematically game the Prisoner's Dilemma problem should be of great concern to the FTC.